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Department of the Treasury  
Washington, DC 20224

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Person To Contact: \_\_\_\_\_, ID No. \_\_\_\_\_

Telephone Number:

Refer Reply To:  
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Date:  
April 16, 2015

In re:

Legend:

Company	=
State	=
Date 1	=
Date 2	=
Year	=
<u>a</u>	=
<u>b</u>	=
<u>c</u>	=
<u>x</u>	=
<u>y</u>	=
<u>z</u>	=
A	=
B	=

Dear \_\_\_\_\_ :

This letter responds to your authorized representative's letter dated October 22, 2014, and subsequent correspondence, concerning the application of § 2703 of the Internal Revenue Code to the proposed transaction.

The facts submitted are as follows. Company is an “S” corporation for federal income tax purposes. The shares of Company are owned outright by (and in trusts for) related

shareholders. The Articles of Incorporation (Articles) for Company were originally filed with State's Secretary of State on Date 1.

Under Article IV, Paragraph 4.1(a) of the Articles, the number of authorized shares of voting common stock of Company is x with a par value of \$a per share. In general, ownership of voting common stock is restricted to a class consisting of: (i) the lineal descendants of A and B, (ii) any shareholder of record as of Date 2, and (iii) certain assignees of Company.

Under Article IV, Paragraph 4.1(b), the number of authorized shares of nonvoting common stock is y with a par value of \$a per share. In general, ownership of nonvoting common stock is restricted to a class consisting of: (i) a person or entity authorized to own voting common stock, (ii) a person or entity approved at the time of transfer by a majority of the Board of Directors, and (iii) a shareholder of record on Date 2.

Paragraph 4.3(a) provides that, with the exception of voting rights, the two classes of common stock are equal and, in the event of dissolution or liquidation, all assets of Company shall be distributed to the common stock.

Since Year (a date before October 8, 1990), the Articles have contained provisions restricting transfers of Company stock. Under Paragraph 4.4, with certain exceptions, any shareholder who desires to transfer the record or beneficial ownership of any shares of voting or nonvoting common stock shall first offer to sell such shares to the Company.

Paragraph 4.6 provides that the Board of Directors has the exclusive authority, at any time, to select particular shares of nonvoting common stock for redemption by paying the fair market value for each share. Under Paragraph 4.5, the fair market value of each share shall be the last appraised value filed with Company by a panel of appraisers.

#### Proposed Transaction

Company has approved a b stock split. Company proposes to amend Paragraph 4.1(b) to authorize the number of nonvoting common stock to be z with a par value of \$a per share. In the transaction, each shareholder will receive a dividend of c nonvoting shares with respect to each outstanding share of common stock (voting and nonvoting) that he or she holds. Paragraph 4.1(a) will continue to authorize the number of voting common shares to be x with a par value of \$a per share.

#### Requested ruling

You have asked us to rule that the stock split, amendment to the Articles, and share dividend will not constitute a substantial modification that would result in the application of § 2703 to the Articles.

### LAW AND ANALYSIS

Section 2703(a) provides that the value of any property shall be determined without regard to (1) any option, agreement, or other right to acquire or use the property at a price less than the fair market value of the property (without regard to such option, agreement, or right), or (2) any restriction on the right to sell or use such property.

Under § 11602(e)(1)(A)(ii) of Public Law 101-508, § 2703 applies to agreements, options, rights, or restrictions entered into or granted after October 8, 1990, and agreements, options, rights, or restrictions in existence prior to October 8, 1990, that are “substantially modified” after that date. See § 25.2703-2.

Section 25.2703-1(c)(1) of the Special Valuation Rules provides that a right or restriction that is substantially modified is treated as a right or restriction created on the date of the modification. Any discretionary modification of a right or restriction, whether or not authorized by the terms of the agreement, that results in other than a *de minimis* change to the quality, value, or timing of the rights of any party with respect to property that is subject to the right or restriction is a substantial modification. If the terms of the right or restriction require periodic updating, the failure to update is presumed to substantially modify the right or restriction unless it can be shown that updating would not have resulted in a substantial modification. The addition of any family member as a party to a right or restriction (including by reason of a transfer of property that subjects the transferee family member to a right or restriction with respect to the transferred property) is considered a substantial modification unless the addition is mandatory under the terms of the right or restriction or the added family member is assigned to a generation (determined under the rules of § 2651 of the Code) no lower than the lowest generation occupied by individuals already party to the right or restriction.

Section 25.2703-1(c)(2) provides that a substantial modification does not include: (i) a modification required by the terms of a right or restriction; (ii) a discretionary modification of an agreement conferring a right or restriction if the modification does not change the right or restriction; (iii) a modification of a capitalization rate used with respect to a right or restriction if the rate is modified in a manner that bears a fixed relationship to a specified market interest rate; and (iv) a modification that results in an option price that more closely approximates fair market value.

In this case, the stock split and amendment to the Articles will apply to all of the common shares (whether voting or nonvoting). Because each shareholder will receive c shares for every common share he or she currently holds, the beneficial interests in Company will not be affected by the stock split, amendment, and share dividend.

Likewise, because the number of authorized voting shares will continue to be x, the shareholders' voting rights will remain unchanged.

Consequently, the stock split, amendment to the Articles, and share dividend will not affect the quality, value or timing of any rights under the Articles, and the changes will not be a substantial modification of the Articles for purposes of § 25.2703-1(c). Accordingly, the Articles will remain exempt from the application of chapter 14.

Except as expressly provided herein, we express no opinion on the federal tax consequences of the transaction under the cited provisions or under any other provisions of the Code.

These rulings are directed only to the taxpayers requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representatives.

The ruling contained in this letter is based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Sincerely,

Leslie H. Finlow  
Senior Technician Reviewer, Branch 4  
Office of Associate Chief Counsel  
(Passthroughs & Special Industries)

Enclosure:  
Copy of letter for § 6110 purposes